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**FISCAL IMPACT STATEMENT**

**LS 7155**

**BILL NUMBER:** HB 1294

**NOTE PREPARED:** Jan 10, 2013

**BILL AMENDED:**

**SUBJECT:** Taxation of Civil Service Annuities.

**FIRST AUTHOR:** Rep. Clere

**FIRST SPONSOR:**

**BILL STATUS:** As Introduced

**FUNDS AFFECTED:** ☒ **GENERAL**  
**DEDICATED**  
**FEDERAL**

**IMPACT:** State & Local

**Summary of Legislation:** This bill increases the allowable state income tax deduction for federal civil service annuity income to the lesser of:

1. The amount of federal civil service annuity income received during the taxable year.
2. The average annual federal Social Security retirement benefit paid to Indiana retired workers during the calendar year preceding the taxpayer's taxable year.

The bill also makes the deduction available to a surviving spouse.

**Effective Date:** January 1, 2013 (retroactive).

**Explanation of State Expenditures:** *Department of State Revenue (DOR):* The DOR will incur additional expenses to revise tax forms, instructions, and computer programs to reflect the changes in this deduction. The DOR's current level of resources should be sufficient to implement this change.

**Explanation of State Revenues:** *Summary* - This bill increases the allowable deduction for federal civil service annuity pay from \$2,000 to the lesser of the actual civil service annuity received or the mean Social Security retirement benefit paid to Indiana retired workers in the prior taxable year. In addition, the bill allows surviving spouses to claim the deduction. Since the bill goes into effect in tax year 2014, the revenue loss would likely begin in FY 2015. The estimated revenue loss from changing the deduction could be about \$6.2 M in FY 2015 and \$6.7 M in FY 2016 (approximately 22.5% attributable to surviving spouses) . The revenue loss could remain relatively flat or grow by as much as 2.9% annually thereafter due to growth in the retiree population

and adjustments to Social Security retirement benefits.

**Background Information** - Under current statute, taxpayers may deduct up to \$2,000 in civil service annuity income. The deduction equals the difference between \$2,000 and the total amount of Social Security or railroad retirement benefits received by the taxpayer. In 2010, 4,546 taxpayers deducted approximately \$7.9 M in civil service annuity pay from their adjusted gross income (AGI). This resulted in a revenue loss of about \$269,000. Based on the current deduction limits and recent annual growth in the deduction, the revenue loss for FY 2015 and FY 2016 is estimated to range from \$269,000 to \$304,000.

Data from the U.S. Office of Personnel Management indicates that there were about 27,000 federal retirees and about 8,000 surviving spouses of federal retirees residing in Indiana. The federal retirees received an estimated \$746 M in annuity payments and surviving spouses received an estimated \$125.1 M in annuity payments during 2012. The average payment to a federal retiree was about \$27,500 and the average for surviving spouses was about \$15,000. The total payments to retirees and their spouses in Indiana increased, on average, 4% over the past 10 years.

According to the Office of Retirement and Disability Policy of the U.S. Social Security Administration (OASDI), the average annual Social Security retirement benefit paid to Indiana retired workers was \$15,476 in year 2011. Since the credit goes into effect for tax year 2013, the average retirement benefit was adjusted for year 2012 and 2013 using the COLA published on the OASDI website. The estimated average Social Security benefit used was \$16,034 for year 2012 and \$16,611 for year 2013.

The estimate relating to civil service annuitants assumes those currently claiming the \$2,000 deduction (4,546 taxpayers) will be able to claim the additional deduction amounts. It also assumes that an additional 16,600 civil service annuitants will be able to claim part or all of the additional deduction. The estimate relating to surviving spouses assumes that survivor's benefits and social security payments to these individuals are distributed similar to civil service annuitants.

**Explanation of Local Revenues:** The change to this tax deduction will likely decrease taxable income, so counties imposing local option income taxes (LOIT) could potentially experience a decrease in revenue. Using the median current LOIT rate of 1.45%, LOIT collections on a statewide basis could potentially be reduced by an estimated \$2.6 M in FY 2015 and \$2.9 in FY 2016.

**State Agencies Affected:** Department of State Revenue.

**Local Agencies Affected:** Counties with local option income taxes.

**Information Sources:** U. S. Social Security Administration, *Social Security Online - Beneficiary Databases*, <http://www.ssa.gov/OACT/ProgData/beniesQuery.html>; LSA Income Tax Databases, 1996-2010; Data on Federal Civil Service Annuitants in Indiana, U.S. Office of Personnel Management (OPM); FEDSCOPE: OPM Personnel Reporting Cube; OASDI, *OASDI Beneficiaries by State and County: Indiana*, May 2012 [http://www.ssa.gov/policy/docs/statcomps/oasdi\\_sc/index.html](http://www.ssa.gov/policy/docs/statcomps/oasdi_sc/index.html)

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